Supreme Court, U.S.
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No. 96-44

In The

Supreme Court of the United States

October Term, 1995

CMC HEARTLAND PARTNERS,

Petitioner,

v.

UNION PACIFIC RAILROAD COMPANY,

Respondent.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Seventh Circuit

RESPONDENT'S BRIEF IN OPPOSITION TO THE PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

This case presents the limited question under Section 77 of the Bankruptcy Act of 1898, formerly 11 U.S.C. § 205 (1976) (repealed 1978) of whether claims based on a statute enacted subsequent to a discharge in bankruptcy are barred by the consummation order. There is no division of the circuits on this issue.

PARTIES TO THE PROCEEDING

Union Pacific Railroad Company is a wholly-owned subsidiary of Union Pacific Corporation. During the pendency of this litigation Union Pacific Railroad Company sold the property which is the subject to this litigation to the Port of Tacoma; in connection with that sale Union Pacific Railroad Company assigned its rights and responsibilities in this litigation to the Port of Tacoma. The Port of Tacoma is a public port district which owns and operates harbor facilities in Tacoma, Washington, and is the real party-in-interest to this litigation. The Court of Appeals declined to substitute parties.

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STATEMENT OF THE CASE

This case is one of many arising out of the bankruptcy of the Chicago, Milwaukee, St. Paul and Pacific Railroad Company ("Milwaukee Road"). That bankruptcy petition was brought and consummated under Section 77 of the Bankruptcy Act of 1898, 11 U.S.C. § 205 (repealed 1978). App. at 21a.

THE RAILYARD

In March of 1980 Union Pacific Railroad Company ("Union Pacific") purchased certain railroad rights-of-way and railyards from the Trustee in Bankruptcy of the Milwaukee Road, including an abandoned railyard in Tacoma, Washington ("Railyard"). Under the terms of the Purchase Agreement Union Pacific received an indemnification from the Trustee, in which the Trustee agreed to indemnify Union Pacific against any and all claims, damages, liabilities, losses or demands whatsoever, regardless of the source or nature thereof, arising out of the operation of the Properties prior to March 12, 1980. App. at 23a.

After the purchase Union Pacific did not operate the Railyard, but did remove the existing structures and track, and cleared the surface of the yard. App. at 5a, 24a. The Railyard sat vacant until 1990 when Union Pacific commissioned a pre-sale environmental audit, which was completed on June 29, 1990. This audit identified subsurface contamination consisting primarily of petroleum hydrocarbons. App. at 27a. This 1990 environmental audit was the first subsurface investigation performed at the Railyard, and as required by law, Union Pacific notified

the Washington Department of Ecology ("Ecology") of the release identified in this assessment. App. at 27a. Based on Union Pacific's notification, Ecology identified Union Pacific as a Potentially Liable Party ("PLP") with respect to subsurface contamination at the Railyard. App. at 27a.

THE PLAN OF REORGANIZATION

Five years before the environmental audit was performed, and the subsurface contamination detected, the Milwaukee Road completed its reorganization and had approved a Plan Of Reorganization. As originally proposed in the draft Plan Of Reorganization, the Scope of The Bar for future claims included claims for contribution and indemnification arising after the consummation date, but which were based on events occurring prior to the consummation date. R. 9, Ex. 12 at 6. The Soo Line Railroad Company and the Milwaukee Road, Inc. (collectively "Soo Line") objected to this provision of the Plan on the grounds that it was unfair, inequitable and discriminatory with respect to certain unliquidated claims. R. 9, Ex. 12. Soo Line requested the Court to modify the Plan to provide for the assumption of contingent and unliquidated claims by the Reorganized Company, so that contingent and unliquidated claims survived the Bar Date. Soo Line cited employees' asbestos-related suits which might be filed in the future as an example of claims which received unfair treatment and which would have required the filing of contingent, unliquidated claims before the bar date. R. 9, Ex. 12 at 5-9. Soo Line asserted that the assumption of contingent, unliquidated claims by

the Reorganized Company was the only way to satisfy the statutory requirement that a reorganization plan under Section 77 of the Bankruptcy Act be fair and equitable. R. 9, Ex. 12 at 12-13.

As a result of these and other objections the Plan of Reorganization was modified to allow for the survival of contingent and unliquidated claims based on facts unknown, undisclosed and unasserted before the bar dates. R. 1, Ex. A at § XI, 11.2. This Amendment was approved by the Court as part of the Plan of Reorganization. R. 1, Ex. A.

On November 2, 1985 the Reorganization Court entered Order No. 866 in the Bankruptcy Proceedings of the Milwaukee Road (the "Consummation Order"); that Order does not enjoin the prosecution or assertion of claims for obligations imposed upon, or required to be assumed by the Reorganized Company, by the Plan or by the Consummation Order. App. at 73a.

PROCEDURAL HISTORY

CMC initially filed a motion for injunctive relief which sought to preclude Union Pacific from pursuing claims for environmental remediation under both the Comprehensive Environmental Response Compensation and Liability Act, 42 U.S.C. § 9601 *et seq.* ("CERCLA") and the Washington Model Toxics Control Act ("Model Act"). After discovery and extensive briefing, on October 21, 1992 the District Court granted CMC's Motion as it pertained to the CERCLA claims, and denied the Motion as it pertained to any claims Union Pacific may have under the Model Act. App. at 37a-38a.

CMC and Union Pacific cross-appealed from the District Court's decision, and the Seventh Circuit affirmed the District Court's decision to the extent it barred Union Pacific's CERCLA claims. With respect to the District Court's holding that Union Pacific's claims under the Model Act survived, the Seventh Circuit acknowledged the general rule that claims based on a subsequently enacted statute are not barred. App. at 33a. Because no finding had been made on CMC's argument that the Model Act did not create new liabilities, the Court remanded the case for a determination: " . . . as to what liabilities under the Model Act existed in 1985 by virtue of Washington state statutes then in effect." App. at 44a-45a, 34a.

On remand, the District Court referred CMC's renewed motion to a Magistrate Judge, who issued a Report and Recommendation ("R&R") which found that the Model Act created an entirely new basis for environmental clean-up liability under Washington state law, and recommended denying CMC's Renewed Motion. App. at 54a-55a. CMC filed objections to the R&R; after briefing and oral arguments the District Court overruled the objections, adopted the R&R (with some minor exceptions) and denied CMC's Renewed Motion. App. at 48a.

On appeal the Seventh Circuit determined that the previously existing Washington statutes did not provide the basis for filing a contingent claim in the bankruptcy proceeding, and affirmed the District Court. App. at 17a.

At no time in the proceedings below did CMC assert or argue the question it seeks to have this Court review.

Similarly, none of the courts below have considered or passed on that question.

REASONS FOR DENYING THE WRIT

I. THE DECISION BELOW IS OF LIMITED PRECEDENTIAL VALUE

CMC urges this Court to grant the writ because of the broad application of the issue at bar, and the sharp division in the circuits over that issue. Contrary to CMC's arguments, the decision below is of limited application because: a) it was decided under the Bankruptcy Act of 1898, which was repealed in 1978 and has a far different definition of claim than the Bankruptcy Code; b) the Plan of Reorganization was specifically modified to allow for the survival of contingent and unliquidated claims; and, c) there is no split in the circuits on this issue, as only two appellate courts have decided the narrow issue present in this case, and those courts are in agreement.

A. Section 77 Of The Bankruptcy Act Defines Claims Narrowly

CMC suggests that a claim under Section 77 of the Bankruptcy Act is the same as a claim under the Bankruptcy Code. This is simply wrong, and a significant distinguishing factor between the Seventh Circuit's decision and the cases cited by CMC. Proceedings under Section 77 of the Bankruptcy Act are unique, as the sole purpose of that section is the reorganization and rehabilitation of the debtor so that it may continue business in

some new form, not the simple liquidation of the debtor's assets and distribution of the proceeds to creditors. *See*, 5 Collier on Bankruptcy § 77.20 (14th Ed. 1978). The Bankruptcy Act generally relies on the concept of provable claims, and allows payment of only those claims which are capable of proof. *In re Edge*, 60 B.R. 690, 694 (Bankr. M.D. Tenn. 1985). Claims not capable of proof are not discharged, and holders of such claims are permitted to pursue the debtor's post-petition assets. *Id.*

Because a Section 77 bankruptcy is like an equitable receivership, and the goal is reorganization, the definition of a Section 77 claim is broader than other sections of the 1898 Act. *See* Bankruptcy Act of 1898, § 77(b), formerly 11 U.S.C. § 205(b) (1976) (repealed 1978). However, the Section 77 definition is far more limited than the definition of claim under the Bankruptcy Code. Under Section 77, unlike other sections of the Act, it is possible to provide for claims which are not "provable" by having the new corporation assume these contingent liabilities. Collier on Bankruptcy § 77.20 (14th Ed. 1978). Even under Section 77, claims not capable of proof are not discharged, and survive the bankruptcy.

The Bankruptcy Code, in a significant departure from the Act, gives the broadest possible definition to claims, and contemplates that all legal obligations of the debtor, no matter how remote or contingent, will be discharged in the bankruptcy case. *See In re Black*, 70 B.R. 645, 648-49 (Bankr. D. Utah 1986) and discussion therein; *see also In re Edge*, 60 B.R. 690, 694 (Bankr. M.D. 1986). Under the Code, even contingent and unliquidated obligations are claims subject to discharge. *See* 11 U.S.C. § 101(4)(A).

It is this latter, broad definition of claim which CMC seeks to have this Court interpret, not the narrower definition of claim under Section 77 of the Bankruptcy Act. The distinctions between these two definitions of claims, and repeal of the Bankruptcy Act, make this case inappropriate for review by this Court.

B. The Plan Of Reorganization Specifically Allows For The Post-Discharge Assertion Of Claims Based On Causes Of Action Arising After The Bar Dates

Consistent with the requirement that a plan of reorganization under Section 77 be fair and equitable, the Milwaukee Road's plan was modified to provide for the survival of contingent and unliquidated claims based on facts unknown, undisclosed and unasserted as of the bar dates. The example given at the time was asbestos-related suits which might be filed in the future, and which upon filing would trigger a right to contribution from the debtor. In the face of these concerns the plan was modified to allow the assertion of claims against the successor corporation even when the cause of action arose after the bar dates, but the relevant conduct occurred before the bar dates.

This plan modification is consistent with how Section 77 manages claims which are not capable of proof at the time of discharge. The claim Union Pacific is now pursuing was not capable of "proof" under Section 77, as Union Pacific could not have reasonably estimated its clean-up liability under a statute which was not yet enacted.

The Seventh Circuit's decision does not give precedence to state law in determining when a claim arises, instead it applies the definition of claim set forth in the plan of reorganization, and properly allows for the survival of this contingent and unliquidated claim. This is not an example of the parade of horribles posited by CMC, but a fair interpretation of the Consummation Order, which exempts from its reach "[o]bligations imposed upon or required to be assumed by the Reorganized Company by the Plan . . . ". App. at 73a. This obligation was imposed on CMC in 1985, when the Plan was approved, not by later action of the Seventh Circuit.

This decision's application is not broad, as CMC argues, but narrow and limited by its own facts. This is not the case in which to consider the broader issues CMC attempts to raise.

C. The Seventh Circuit And The Third Circuit Agree On When A Claim Based On A Later Enacted Statute Arises

Only the Third and Seventh Circuit Courts of Appeal have addressed the issue of when a claim based on a statute adopted after the bar dates arises. *See In re Penn Central Transportation Co.*, 944 F.2d 164 (3d Cir. 1992), *cert. denied*, 503 U.S. 906 (1992); App. at 3a. Both of those courts concluded that claims based on a statute enacted after the discharge date are not barred. *Id.* Significantly, both of these decisions were decided under Section 77 of the Bankruptcy Act of 1898, not the Bankruptcy Code.

In contrast, none of the other cases cited by CMC concern a later enacted statute, and all of these cases were

decided under the Bankruptcy Code of 1978, 11 U.S.C. § 101, *et seq. See In re Piper Aircraft Corp.*, 58 F.3d 1573, 1574 (11th Cir. 1995); *In re Jensen*, 995 F.2d 925, 927 (9th Cir. 1993); *Grady v. A.H. Robbins Co.*, 839 F.2d 198, 199 (4th Cir. 1988), *cert. dismissed*, 487 U.S. 1260 (1988).

These courts criticize the Third Circuit's formulation of when a claim arises as stated in the case of *In re Frenville Co.*, 744 F.2d 332 (3d Cir. 1984), *cert. denied*, 469 U.S. 1160 (1985), not the Seventh Circuit's formulation in this case or the Third Circuit's holding in *Penn Central*. *Frenville*, like the cases criticizing it, was decided under the Bankruptcy Code, under the Bankruptcy Act, and did not concern a later enacted statute. *Id.* at 333.

The "split in authority" postulated by CMC simply does not exist in this case. Only the Third and Seventh Circuit Courts of Appeal have decided this issue; both are in agreement and neither relied on *Frenville* or the rationale of that case. This case is not *Frenville*, does not rely on *Frenville*, and should not be reviewed because some courts disagree with *Frenville*.

II. THE QUESTION PRESENTED BY THE PETITIONER WAS NOT PRESSED OR PASSED ON IN THE COURTS BELOW

CMC urges this Court to review the decision below on an issue which was not presented to either the District Court or Court of Appeals, and on which neither passed. This request ignores the traditional rule of this Court, which usually declines to consider questions presented in a petition for certiorari which have not been considered by the lower court. *Youakim v. Miller*, 425 U.S. 231, 234, 96

S.Ct. 1399, 1401, 47 L.Ed. 2d 701 (1976) (per curiam). This Court will generally review a question not raised in the courts below only in exceptional circumstances. *Duignan v. United States*, 274 U.S. 195, 200, 47 S.Ct. 566, 568, 71 L.Ed. 996 (1927). There are no exceptional circumstances here, and this Court should decline to review this matter.

A. First Ruling Of The District Court

On its initial Motion for Injunctive Relief CMC argued that: "[s]ince Union Pacific could have brought a CERCLA claim before the bar dates, and did not, it should be barred from bringing a similar state law claim although the state statute was not in effect at the time of the reorganization." App. at 44a. The District Court denied CMC's request to bar Union Pacific's state law claim, relying on *In re Penn Central*, 944 F.2d 164 (3d Cir. 1991), *cert. denied*, 503 U.S. 906 (1992) (finding that claim for CERCLA remediation costs was not discharged in bankruptcy when the consummation order was entered before CERCLA was enacted). App. at 44a-45a. The District Court reasoned that Union Pacific could not have known of its claim under a statute which was not enacted as of the bar date. App. at 44a. This fundamental holding has never been challenged by CMC; instead, its argument since that time has been limited to whether previously existing Washington State statutes imposed similar liabilities on Union Pacific.

B. First Appeal To The Seventh Circuit

On CMC's appeal from the order of the District Court, it argued that the Model Act was essentially a recodification of other Washington state statutes, and that those existing statutes imposed clean-up liability on Union Pacific before the bar dates. App. at 29a, 33a. The District Court had made no findings with respect to that argument (as it was not presented to the court), and the Seventh Circuit remanded the case for a determination of "[w]hether a particular type of liability under the Model Act existed under predecessor statutes prior to the bar dates, and whether Union Pacific consequently had a contingent claim for environmental clean-up costs under Washington statutes in effect before the bar dates." App. at 34a.

C. Proceedings On Remand

The District Court referred the matter to a Magistrate Judge for determination of this narrow issue. The Magistrate Judge issued a Report and Recommendation ("R&R") which compared Union Pacific's liability under the Model Act with its liability under earlier existing Washington State statutes, and concluded the earlier statutes did not impose liability on Union Pacific. App. at 54a-55a. CMC objected to the R&R on the grounds that the Magistrate Judge: 1) assumed facts not in the record; 2) misapplied the Seventh Circuit's standard pertaining to a definition of claim under the Bankruptcy Act; and, 3) improperly interpreted Washington state law. App. at 47a.

The District Court rejected CMC's arguments and adopted the R&R with minor exceptions. App. at 48a. With respect to the definition of claim CMC did not argue, as it does now, that the claim arose at the time the conduct occurred. Instead, CMC argued that the proper test under Section 77 is whether Union Pacific had a contingent claim based on the possible liability Union Pacific could have faced under other state laws. App. at 50a. In rejecting CMC's argument regarding the proper test under Section 77, the District Court examined the definition of claim under Section 77 of the Bankruptcy Act and the Seventh Circuit's direction on remand. App. at 51a-55a. The District Court did not examine, and did not reach, the issue of whether the claim arose when the underlying conduct occurred, as that issue was never raised by CMC. *Id.*

D. Second Appeal To The Seventh Circuit

On appeal CMC once again argued that the previously existing Washington State statutes imposed liability on Union Pacific so that a later claim based on the Model Act was barred. App. at 9a. CMC's argument, and the Seventh Circuit's opinion, focused on the comparison between the Model Act and other Washington statutes; CMC did not argue, and the Court did not address, the question of whether the claim arose when the underlying conduct occurred. App. at 1a-18a.[1]

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[1] CMC did file a Petition for Rehearing and Suggestion for Rehearing En Banc in which it argued that this decision misapplied the earlier definition of claim established by the

The question raised by CMC now was not presented to either the District Court or to the Seventh Circuit Court of Appeals. This new argument, formulated in a last ditch effort to "save the day" after defeat below, should not be considered by this Court. There are no unusual circumstances or compelling reasons to break with this Court's tradition of declining to review questions not pressed or passed on by the courts below. The writ should be denied.

CONCLUSION

The "parade of horribles" feared by CMC will not flow from the Seventh Circuit's decision. This case was decided under Section 77 of the Bankruptcy Act of 1898 (repealed 1978), and based on a plan of reorganization which specifically provides for the survival of contingent and unliquidated claims. The narrow issue of whether claims based on a statute adopted after the discharge date are barred has been addressed by only two circuits, which agree such claims are not. Additionally, the issue as now framed by CMC was not raised in or addressed by the courts below.

Seventh Circuit, and that the decision elevated state law over federal bankruptcy law. However, that is a far different issue from the question CMC now presents.

For the foregoing reasons the petition for a writ of certiorari to the United States Court of Appeals for the Seventh Circuit should be denied.

Respectfully Submitted,

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